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No. 80-[illegible]

IN THE

Supreme Court of the United States

OCTOBER TERM, 1980

SHELDON BASUCH TOBES,
Petitioner,

v.

STUART J. RADLOFF, TRUSTEE,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Eighth Circuit

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BRIEF OF AMICUS CURIAE IN SUPPORT OF THE JUDGMENT BELOW

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QUESTION PRESENTED

Whether a consumer debtor who is not engaged in an ongoing business may proceed under Chapter 11 of the Bankruptcy Code, 11 U.S.C. § 1101 *et seq.*, which is designed to allow business reorganizations.

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STATEMENT OF FACTS

In this case an individual consumer debtor, who does not operate a business, contends that Chapter 11 of the Bankruptcy Code,[1] which plainly was intended and designed to govern *business* reorganizations, is available to him and others in comparable straits.

From March 1983 until he was terminated in April 1985, Petitioner served as a consultant to the Independence Electric Corporation ("IEC") earning $50,000 per year plus expenses. Pet. App. A21.[2] IEC is a privately

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[1] 11 U.S.C. § 1101 *et seq.*

[2] The Appendix filed by Petitioner with his Petition for a Writ of Certiorari is cited as "Pet. App." The Joint Appendix filed herein is cited as "J.A." Petitioner's Brief is cited as "Pet. Br." The Brief of Respondent Stuart J. Radloff, the Chapter 7 Trustee, is cited as "Resp. Br."

held corporation organized to explore alternative energy opportunities. IEC's stock is owned by three individuals, including Petitioner who holds 24 percent of its shares. J.A. 129, 131-132. Since he lost his position with IEC in April 1985, Petitioner has had no regular source of income. His parents and friends have supported him. J.A. 58, 147.

Petitioner originally filed a voluntary petition for relief under Chapter 7 of the Bankruptcy Code [3] on November 18, 1986. Pet. App. A19. Petitioner filed under Chapter 7 because he thought his IEC stock "was totally worthless and the company was dead." *Id.* at 141. His filing disclosed (i) no secured debts, (ii) a disputed federal tax priority claim of $11,000, and (iii) unsecured debts of $170,605. He listed his non-exempt assets as his IEC stock and a "possible claim against business associates for breach of duty," but stated that the market value of both was "unknown." Schedules of Assets and Liabilities, Schedules A-1, A-3 and B-2 (October 30, 1986).

On August 6, 1987, Stuart Radloff, the Chapter 7 Trustee appointed to administer Petitioner's estate, notified Petitioner's creditors that the IEC Board of Directors had offered to purchase his stock for $25,000. J.A. 13-14. Realizing the stock had some value and solely to avoid its liquidation, Petitioner moved to convert his Chapter 7 case to one under Chapter 11. J.A. 15, 18, 150. The bankruptcy court granted the motion on October 2, 1987. J.A. at 21.

In his Chapter 11 Schedules of Assets and Liabilities, Petitioner listed a disputed federal tax priority claim of $4,200 and unsecured debts of $137,619. J.A. 64. Again, the only non-exempt assets he identified were his IEC stock and the possible claim against business associates, both having "unknown" value. *Id.* at 55, 12. He showed no income from any source other than his parents, who

[3] 11 U.S.C. §§ 701 *et seq.*

paid his monthly expenses. J.A. 57-58. Petitioner had no operating business to preserve, no employees to protect, and no business assets used in the production of income. Pet. App. A24-A28.

Petitioner filed a reorganization plan that proposed to pay his unsecured creditors $25,000, less administrative expenses and priority tax claims, which would result in an actual payment to unsecured creditors of approximately 11 cents on the dollar. He proposed to obtain the $25,000 to fund the plan by an unsecured loan from an unspecified source. He further proposed to pay unsecured creditors 50 percent of the dividends he might receive from his IEC stock and 50 percent of any proceeds from the sale of this stock during a six year period up to the principal amount of their claims, and also 100 percent of any amounts he might recover from his claims against his IEC associates. J.A. 76-77, 92-94, 114-115.

After notice and a hearing, the bankruptcy court ordered Petitioner either to convert his case to one under Chapter 7 or face dismissal. Pet. App. A17-A28. Relying on *Wamsganz v. Boatmen's Bank of De Soto*, 804 F.2d 503 (8th Cir. 1986), the court held that Petitioner did not qualify as a debtor under Chapter 11 because he was not engaged in an ongoing business that he sought to reorganize under protection of the bankruptcy laws. Pet. App. A27-A28. Upon Petitioner's refusal to convert to Chapter 7, the court dismissed the case. The District Court for the Eastern District of Missouri affirmed the bankruptcy court's decision, as did the Eighth Circuit Court of Appeals. *Id.* at A8-A16, A2-A7. This Court granted his Petition for a Writ of Certiorari on January 18, 1991. On January 22, 1991, the Court appointed undersigned counsel *amicus curiae* in support of the judgment below.

SUMMARY OF ARGUMENT

An individual debtor not engaged in an ongoing business does not qualify for relief under Chapter 11 of the Bankruptcy Code. Section 109 of the Code sets forth certain broad eligibility requirements for debtors under various Chapters of the Code. The Code, however, must be read as a whole and those eligibility requirements are further qualified by the provisions of each Chapter. For example, according to the definition in Section 109(b), a person may be a debtor under Chapter 7 "only if" the person is not one of certain specified entities. However, Sections 707(b) and 727(a) deny Chapter 7 relief to consumer debtors who are able to pay their debts or who have been granted a Chapter 7 discharge within six years. Similarly, although Section 109(d), which defines who may be a debtor under Chapter 11, contains no explicit on-going business requirement, such a requirement is evident from the provisions of Chapter 11. Reading the Code as a whole shows that Section 109, by eliminating certain debtors from those who may proceed under Chapters 7 and 11, does not automatically encompass all others.

Chapter 11 is specifically tailored to allow the reorganization of an on-going business, not the rehabilitation of a consumer debtor. The Chapter's fundamental provisions have no applicability in the consumer debtor context. Numerous courts thus have concluded that a debtor who does not have a viable business to restructure or employees to protect is not entitled to seek Chapter 11 relief.

The Code's legislative history requires this interpretation of the statute. The House Report conclusively demonstrates that Chapters 7 and 13 are the "only remed[ies]" available to consumer debtors. H.R. Rep. No. 595, 95th Cong., 2d Sess. 125 (1977), *reprinted in* 1978 U.S. Code Cong. & Admin. News 5963, 6086. The Senate Report states that "Chapter 11 deals with the reorganization of

a financially distressed business enterprise." S.Rep. No. 989, 95th Cong., 2d Sess. 9 (1978), *reprinted in* 1978 U.S. Code Cong. & Admin. News 5787, 5795.

Other provisions of the Bankruptcy Code demonstrate that Chapter 11 is not intended for use by consumer debtors. Consumer debtors may *not* be forced into involuntary bankruptcy under Chapter 13,[4] which provides for the use of disposable income to repay creditors. The statute bars involuntary Chapter 13 petitions because an unwilling debtor cannot be forced to repay his creditors. Creditors, however, may force debtors into involuntary bankruptcy under Chapter 11. If Chapter 11 applies to consumer debtors, such debtors could be forced into involuntary reorganization plans, despite the fact that they would be no more likely to cooperate in such plans than Chapter 13 debtors would be to cooperate in involuntary repayment plans.

Allowing consumer debtors to use Chapter 11 is inconsistent with its purposes. Chapter 11 authorizes the reorganization of financially troubled business enterprises in order to keep them in operation, preserve jobs and protect investors. No such purposes would be served by permitting consumer debtors to reorganize under Chapter 11. Consumer debtors may seek relief under Chapter 7 or Chapter 13 of the Bankruptcy Code. Chapter 11 should not be made available to consumer debtors, such as Petitioner, merely because they cannot qualify under Chapter 13 and wish to avoid Chapter 7 liquidation.

Indeed, allowing consumer debtors to proceed under Chapter 11 would permit them both to protect their nonexempt assets *and* their postpetition disposable income—an expansive beneficial result not provided by any other Chapter that Congress evidently did not intend. If consumer debtors thought they might gain such protections under Chapter 11, the bankruptcy courts might well be

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[4] 11 U.S.C. § 1301 *et seq.*

inundated with attenuated, unworkable plans from such debtors.

ARGUMENT

The Eighth Circuit correctly held that Petitioner, an individual debtor not engaged in an ongoing business, is not eligible for Chapter 11 relief. The Fifth and Sixth Circuits similarly have determined that Chapter 11 is designed "to assist financially distressed business enterprises by providing them with breathing space in which to return to a viable state," and is not available to an individual consumer debtor with no business to reorganize. *In the Matter of Little Creek Development Co.*, 779 F.2d 1068, 1073 (5th Cir. 1986); *In the Matter of Winshall Settlor's Trust*, 758 F.2d 1136, 1137 (6th Cir. 1985). Petitioner's contention that individuals without businesses may proceed under Chapter 11 is not supported by the language of the Bankruptcy Code, its legislative history, or the policy underlying it.

I. THE BANKRUPTCY CODE, READ AS A WHOLE, DOES NOT ALLOW EVERY INDIVIDUAL DEBTOR TO PROCEED UNDER CHAPTER 7 OR 11

Section 109 of the Bankruptcy Code defines who may be a debtor under its various chapters. 11 U.S.C. § 109. Section 109(b) provides that a person may be a debtor under Chapter 7 "only if" the person is not a railroad, banking institution or insurance company. Section 109(d) provides that "only a person" that may be a debtor under Chapter 7 (except a stockbroker or commodity broker) and a railroad may be a debtor under Chapter 11. Because Section 109(d) does not explicitly preclude individuals who are not engaged in business from qualifying as debtors under Chapter 11, Petitioner and Respondent contend that the statute plainly grants all individuals the right to proceed under Chapter 11. Pet. Br. at 10-12; Resp. Br. at 9-12.

The issue, however, is not as simple as Petitioner and Respondent would have the Court conclude. When Section 109(b) and (d) are read in conjunction with other provisions of the Bankruptcy Code, it becomes clear that not all individual debtors are entitled to proceed under Chapters 7 or 11. Certain individual debtors, for example, are not entitled to proceed under Chapter 7, despite the fact that they are not specifically precluded from so doing by the language of Section 109(b). In other words, as shown momentarily, Section 109(b), by eliminating some debtors from its coverage, does not automatically encompass all others in the category that may proceed under Chapter 7.

First, however, we mention a commonplace of statutory interpretation. " 'The true meaning of a single section of a statute . . . cannot be ascertained if it be considered apart from related sections. . . .' " *Commissioner of Internal Revenue v. Engle*, 464 U.S. 206, 223 (1984) (quoting *Helvering v. Morgan's, Inc.*, 293 U.S. 121, 126 (1934)). In construing a statute, " 'the court will not look merely to a particular clause in which general words may be used, but will take in connection with it the whole statute . . . and the objects and policies of the law. . . .' " *Stafford v. Briggs*, 444 U.S. 527, 535 (1980) (quoting *Brown v. Duchesne*, 19 How. 183, 194 (1857)). *See, Richards v. United States*, 369 U.S. 1, 11 (1962) ("a section of a statute should not be read in isolation from the context of the whole Act"). With respect to the Bankruptcy Code, this Court recently confirmed that "[s]tatutory construction . . . is a holistic endeavor" and the meaning attributed to a particular provision must produce a substantive effect consistent with related provisions of the Code. *United Savings Ass'n of Texas v. Timbers of Inwood Forest Assoc., Ltd.*, 484 U.S. 365, 371 (1988). The bankruptcy laws, this Court has said, must not be interpreted in a way that leads to "absurd or futile results." *Perry v. Commerce Loan Co.*, 383 U.S. 392, 400 (1966) (quoting *United States v. American Trucking Ass'ns.*, 310 U.S. 534, 543 (1940)).

Contrary to the assertions of Petitioner and Respondent (Pet. Br. at 11-12; Resp. Br. at 10-12), the Section 109 restrictions on a person's eligibility to proceed under various chapters of the Bankruptcy Code are *not* exclusive. For example, an individual who qualifies as a Chapter 7 debtor under Section 109(b), but whose debts are primarily consumer debts that he is able to pay, will be denied use of Chapter 7 pursuant to 11 U.S.C. § 707(b), because the grant of liquidation relief in such circumstances would constitute a "substantial abuse of the provisions of this chapter."[5] *See, In re Walton*, 866 F.2d 981, 984-985 (8th Cir. 1989) (consumer debtor who has ability to repay creditors not entitled to voluntary Chapter 7 relief); *In re Krohn*, 886 F.2d 123, 127 (6th Cir. 1989) (consumer debtor's ability to repay debts justifies denial of access to Chapter 7 relief); *In re Kelly*, 841 F.2d 908, 915 (9th Cir. 1988) (consumer debtor's ability to repay debts for which discharge is sought precludes Chapter 7 relief). In addition, a person qualifying as a Chapter 7 debtor under Section 109(b) is barred from obtaining relief if he has been granted a Chapter 7 or Chapter 11 discharge in a case commenced within six years of the current filing. *See* 11 U.S.C. § 727(a)(8).

Similarly, as now shown, a consumer debtor who is not engaged in business is not qualified to proceed or obtain relief under the reorganization provisions of Chapter 11. To allow such a person to commence a Chapter 11 case just because he is not expressly excluded by Section 109(d)'s threshold definition would be a futile gesture.

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[5] Section 707(b) authorizes the court to dismiss a Chapter 7 case in such a situation. It does *not* provide for reorganization as Respondent suggests. (Resp. Br. at 14).

II. THE LANGUAGE OF CHAPTER 11 DEMONSTRATES CONCLUSIVELY THAT IT WAS DESIGNED AND INTENDED FOR BUSINESS DEBTORS, NOT CONSUMER DEBTORS

The provisions of Chapter 11 are plainly tailored to allow and facilitate the reorganization of an ongoing business, not the rehabilitation of an individual consumer debtor. For example:

- Section 1102(a)(1) of Chapter 11 authorizes the appointment of an *equity security holders* committee.
- Section 1103(c)(2) authorizes a committee appointed under Section 1102 to "investigate . . . the operation of the debtor's *business* and the desirability of the continuance of such *business*. . . ." (emphasis added)
- Section 1104 authorizes the court to order the appointment of a trustee "for cause, including fraud, dishonesty, incompetence, or *gross mismanagement of the affairs of the debtor by current management*. . . ." (emphasis added)
- Section 1105 authorizes the court to terminate a trustee's appointment and "restore the debtor to possession and management of the property of the estate and of the operation of the debtor's *business*." (emphasis added)
- Section 1106(a)(3) authorizes a trustee to "investigate . . . the operation of the debtor's *business* and the desirability of the continuance of such *business*. . . ." (emphasis added).
- Pursuant to Sections 1107(a) and 1108, the debtor-in-possession or the trustee is authorized to "operate the debtor's *business*."
- Section 1113 addresses collective bargaining agreements and Section 1114, the payment of insurance benefits to retired employees.

- Pursuant to Section 1141(d)(3), a debtor is not discharged by the confirmation of a plan if the plan provides for liquidation of all or substantially all of the property of the estate and "the debtor *does not engage in business* after consummation of the plan."

These basic provisions have absolutely no applicability in the consumer debtor context. Rather, they demonstrate that Chapter 11 was intended and designed for financially troubled business enterprises endeavoring to continue in operation while they restructure their debts. *See Winshall Settlor's Trust*, 758 F.2d 1136, 1137.

Although the Bankruptcy Code does not explicitly require that a Chapter 11 debtor have an ongoing business, numerous courts properly have held that such a requirement is inherent and implied in the provisions of that Chapter. *See, e.g., Wamsganz v. Boatmen's Bank of DeSoto*, 804 F.2d 503 (8th Cir. 1986); *In the Matter of Little Creek Development Co.*, 779 F.2d 1068 (5th Cir. 1986); *In the Matter of Winshall Settlor's Trust*, 758 F.2d 1136 (6th Cir. 1985); *In re Lange*, 75 Bankr. 154 (Bankr. N.D. Ohio 1987); *In re Roland*, 77 Bankr. 265 (Bankr. D. Mont. 1987); *In re Bendig*, 74 Bankr. 47 (Bankr. D. Conn. 1987); *In re Penn Realty Trust*, 4 Bankr. 226 (Bankr. D. Mass. 1980). "[I]f there is not a potentially viable business in place worthy of protection and rehabilitation, the Chapter 11 effort has lost its *raison d'etre* . . . ." *Winshall Settlor's Trust*, 758 F.2d at 1137 (quoting *In re Ironsides, Inc.*, 34 Bankr. 337, 339 (Bankr. W.D. Ky. 1983)).

A debtor must act in good faith in filing a voluntary Chapter 11 petition and the failure to do so may constitute cause for dismissal under 11 U.S.C. § 1112(b). Among the factors courts examine in determining whether a debtor has petitioned in good faith is whether the debtor is engaged in an ongoing business that can be reorganized as contemplated by the statute. *Winshall*

Settlor's Trust, 758 F.2d at 1137; *Wamsganz*, 804 F.2d at 540-505; *Little Creek Development Co.*, 779 F.2d at 1073. Where a debtor does not have a viable business to restructure or employees to protect, he should not be afforded Chapter 11 reorganization relief.[6] *Id.*

III. THE LEGISLATIVE HISTORY CONCLUSIVELY CONFIRMS WHAT THE BANKRUPTCY CODE ITSELF DEMONSTRATES—THAT CHAPTER 11 IS INTENDED SOLELY FOR BUSINESS REORGANIZATIONS

The legislative history of the Bankruptcy Code shows that ongoing business enterprises are the intended candidates for Chapter 11 reorganization relief. Indeed, the House Report demonstrates conclusively that Chapters 7 and 13 provide the "only remed[ies]" available to consumer debtors.

The Senate Report unambiguously provides that:

> Chapter 11 deals with the *reorganization of a financially distressed business enterprise*, providing for its rehabilitation by adjustment of its debt obligations and equity interests.
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> • • • •

[6] In *In re Moog*, 774 F.2d 1073 (11th Cir. 1985), the Eleventh Circuit held that a consumer debtor is eligible for relief under Chapter 11. The debtor there had no regular source of income and consequently could not qualify for Chapter 13. Her sole asset was her personal residence valued at $269,000 and subject to mortgages totalling $160,000. Her debts, all of a consumer nature, totalled $16,000. The court determined that the debtor should be permitted to proceed under Chapter 11 so that she would not be forced to liquidate her home to repay her creditors. This decision, however, is inconsistent with 11 U.S.C. § 522, which specifies the property a debtor may exempt from the bankruptcy estate. Although Section 522(d)(1) allows a debtor to exempt a portion of her equity interest in her personal residence, the Code does not authorize a wholesale homestead exemption. Nonetheless, the *Moog* court improperly sanctioned a consumer debtor's use of Chapter 11 in a manner that would defeat the limitations of Section 522(d)(1).

> Reorganization, in its fundamental aspects, involves the thannkless task of determining who should share the losses incurred by an *unsuccessful business* and how the values of the estate should be apportioned among creditors and stockholders.

S. Rep. No. 989, at 9, 10 (1978), *reprinted in* 1978 U.S. Code Cong. & Admin. News at 5795, 5796 (emphasis added).

Both the House and Senate Reports describe Chapter 11 as a single, consolidated "chapter for all business reorganizations." S. Rep. No. 989 at 9, *reprinted in* 1978 U.S. Code Cong. & Admin. News at 5795; H.R. Rep. No. 595, at 223 (1977), *reprinted in* 1978 U.S. Code Cong. & Admin. News at 6183. The House Report further explicates the basis of the Chapter 11 reorganization provisions:

> The purpose of a business reorganization case, unlike a liquidation case, is to restructure a business's finances so that it may continue to operate, provide its employees with jobs, pay its creditors, and produce a return for its stockholders. The premise of a business reorganization is that assets that are used for production in the industry for which they were designed are more valuable than those same assets sold for scrap. Often, the return on assets that a business can produce is inadequate to compensate those who have invested in the business. Cash flow problems may develop, and require creditors of the business, both trade creditors and long-term lenders, to wait for payment of their claims. If the business can extend or reduce its debts, it often can be returned to a viable state. It is more economically efficient to reorganize than to liquidate, because it preserves jobs and assets.

H.R. Rep. No. 595 at 220, *reprinted in* 1978 U.S. Code Cong. & Admin. News at 6179.

None of these considerations applies to an individual consumer debtor. A consumer debtor has no employees,

no jobs to preserve and no assets used in the business that might be more valuable on a going concern basis than when sold for scrap. Consumer debtors *are not even mentioned* in the chapter of the House Report devoted to reorganization. H.R. Rep. No. 595 at 220-262, *reprinted in* 1978 U.S. Code Cong. & Admin. News at 6179-6220.

Even more significantly, the House Report shows that the only chapters of the Bankruptcy Code that are available to consumer debtors are Chapters 7 and 13:

> The premises of the bill with respect to consumer bankruptcy are that use of the bankruptcy law should be a last resort; that if it is used, debtors should attempt repayment under chapter 13, Adjustment of Debts of an Individual with Regular Income; and finally, whether the debtor uses chapter 7, Liquidation, or chapter 13, Adjustment of Debts of an Individual, bankruptcy relief should be effective, and should provide the debtor with a fresh start.
>
> . . . .
>
> Some consumer debtors are unable to avail themselves of the relief provided under chapter 13. For these debtors, *straight bankruptcy is the only remedy that will enable them to get out from under the debilitating effects of too much debt.*

H.R. Rep. No. 595 at 118, 125, *reprinted in* 1978 U.S. Code Cong. & Admin. News at 6078-6079, 6086 (emphasis added). This passage shows beyond peradventure that consumer debtors may seek relief only under Chapters 7 and 13, and may not avail themselves of the protections of Chapter 11.[7]

To support their arguments that the legislative history reflects Congress' intent to make Chapter 11 available to nonbusiness debtors, Petitioner and Respondent cite the following passage from the Senate Report:

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[7] Chapter 11's legislative history is discussed at length in the *Wamsganz case*, 804 F.2d at 505.

> Chapter 11, Reorganization, is primarily designed for businesses, although individuals are eligible for relief under the chapter. The procedures of chapter 11, however, are sufficiently complex that they will be used only in a business case and not in the consumer context.

S. Rep. No. 989 at 3, *reprinted in* 1978 U.S. Code Cong. & Admin. News at 5789.

A similar statement is found in the House Report:

> Chapter 11, Reorganization, is primarily designed for businesses, but permits individuals to use the chapter. The procedures of chapter 11, however, are sufficiently burdensome that their use will only make sense in the business context, and not in the consumer context.

H.R. Rep. No. 595 at 6, *reprinted in* 1978 U.S. Code Cong. & Admin. News at 5968.

These statements are ambiguous at best and, when read with the legislative history just reviewed, should be interpreted to indicate that only individuals *operating businesses* may use Chapter 11 and that consumer debtors may not.[8] In any event, as these excerpts show, Congress clearly did *not* anticipate that consumer debtors would employ Chapter 11.[9]

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[8] Even Petitioner is forced to concede that the legislative history he cites to support his position is "less than conclusive." Pet. Br. at 19.

[9] Petitioner also cites a passage in the House Report discussing a provision making Chapter 13 available to sole proprietors in addition to wage earners, a change from pre-Code law. Pet. Br. at 19. The passage states that the House bill offered "small sole proprietors as well as wage earners an alternative to Chapter 11." Petitioner contends that this phrase constitutes an acknowledgement that Chapter 11 is available to persons without a business. Again, this imprecise passage is subject to varying interpretations—in context it might be read to mean only that sole proprietors, like wage earners, may use Chapter 13. Such an interpretation is preferable given the clear pronouncement in the House Report, quoted above, that only Chapters 7 and 13 are available to consumer debtors. Even if the conclusion is that the passage Petitioner quotes is inconsistent with the House statement we rely on, we submit that the far more definitive statement we cite should be given greater weight.

IV. OTHER BANKRUPTCY CODE PROVISIONS, INCLUDING THOSE IN CHAPTER 13, DEMONSTRATE THAT CHAPTER 11 WAS NOT INTENDED TO PROVIDE RELIEF TO CONSUMER DEBTORS

Chapter 13 permits an individual debtor to retain his assets and repay his creditors out of future disposable income. 11 U.S.C. § 1306. However, 11 U.S.C. § 303(a) prohibits the filing of an involuntary Chapter 13 petition against an individual consumer debtor. Involuntary petitions are not permitted because Chapter 13 "only works when there is a willing debtor who wants to repay his creditors." S. Rep. No. 989 at 32, *reprinted in* 1978 U.S. Code Cong. & Admin. News at 5818. Similarly, creditors are not permitted to force a voluntary Chapter 13 debtor into an involuntary repayment plan because an unwilling debtor is unlikely to cooperate in such a plan. 11 U.S.C. § 1321; H.R. Rep. No. 595 at 123, *reprinted in* 1978 U.S. Code Cong. & Admin. News at 6084.

In contrast, involuntary petitions may be filed to force a debtor into a Chapter 11 proceeding. 11 U.S.C. § 303(a). Moreover, if a Chapter 11 debtor fails to file a reorganization plan in a timely manner or to file an acceptable plan, any party in interest may propose a plan. 11 U.S.C. § 1121(c). If Chapter 11 is construed to apply to individual consumer debtors, such debtors could be forced into involuntary Chapter 11 proceedings and reorganization plans.

A putative Chapter 11 consumer debtor, however, would be similarly situated to a Chapter 13 debtor and would be no more likely to cooperate in an involuntary reorganization plan than a Chapter 13 debtor would be to cooperate in an involuntary repayment plan. It thus

makes no sense to construe Chapter 11 to encompass consumer debtors and to subject them to involuntary reorganization plans.

Examination of the reorganization plan Petitioner has proposed emphasizes this point. Petitioner's plan would have him borrow $25,000 to pay his creditors what they would receive if his sole asset—his IEC stock—was sold in liquidation. But surely, even if his creditors could force him into Chapter 11, they could not compel him to incur further debt, as he proposes, or essentially do anything else to effectuate payment except liquidate his IEC stock. Similarly, in *In re Moog*, 774 F.2d 1073 (11th Cir. 1989)—a case heavily relied on by both Petitioner and Respondent—the creditors could not have forced the petitioner to enter into a viable repayment plan.[10]

Pursuant to 11 U.S.C. § 1307(d), a court may convert a case under Chapter 13—which also applies to certain business debtors—to a Chapter 11 case at the request of any party in interest or the trustee. The House Report counsels that a court shall "excercise its sound discretion in determining whether to grant the request, based on *the nature of the debtor's business* and other similar factors." H.R. Rep. No. 595 at 428, *reprinted in* 1978 U.S. Code Cong. & Admin. News at 6384. Thus, the House clearly contemplated that a Chapter 13 case could be converted to a Chapter 11 case only where the debtor was engaged in an on-going business.

Finally, we observe that Chapter 13 is available only to those consumer debtors who, unlike Petitioner, have regular income and unsecured debts of less than $100,000. 11 U.S.C. § 109(e). Why Congress imposed this limitation on consumer debtors is not wholly clear,[11] but it

[10] Even the *Moog* decision notes that Chapter 11 is "primarily aimed at business debtors." 774 F.2d at 1074.

[11] The limitation, in part, was intended "to prevent sole proprietors with large businesses from abusing creditors by avoiding

seems fair to conclude that Congress intended that consumer debtors with such large debts should be limited to liquidation and should not be allowed to propose and effect either a repayment or reorganization plan.

V. PETITIONER'S ARGUMENT BASED ON FORMER PROVISIONS OF THE BANKRUPTCY ACT IS UNPERSUASIVE

Petitioner asserts that the practice under Chapter XI of the Bankruptcy Act—one of the predecessor provisions to the current Chapter 11—permitted consumer debtors to reorganize. Petitioner contends that, because the legislative history does not indicate Congress's intent to depart from this practice, "it should be presumed that Congress intended to continue that practice in the codification of Chapter 11 and that Congress intended that Chapter 11 be made available to nonbusiness individual debtors." Pet. Br. at 13.

The legislative history of the Bankruptcy Code, however, is devoid of any congressional recognition of a "practice" permitting consumer debtors to reorganize under former Chapter XI of the Bankruptcy Act. Indeed, the House Report expressed the concern that the Bankruptcy Act did not provide an effective remedy to consumer debtors who were often forced to liquidate because the restrictions on relief and limitations on eligibility found in former Chapter XIII discouraged or precluded them from attempting to negotiate repayment plans with creditors. There is no mention of former Chapter XI as an alternative available to consumer debtors. H.R. Rep. No. 595 at 116-125, *reprinted in* 1978 U.S. Code Cong. & Admin. News at 6076-6086. Rather, Chapter XI was identified as one of "four chapters [designed] for the reorganization of businesses." H.R. Rep.

Chapter 11." H.R. Rep. No. 595 at 119, *reprinted in* 1978 U.S. Code Cong. & Admin. News at 6080. This does not explain the limitation as to consumer debtors who do not operate a business.

No. 595 at 221, *reprinted in* U.S. Code Cong. & Admin. News at 6181.

Chapter VIII (Section 77) of the Bankruptcy Act, dealt with railroad reorganizations, Chapter X provided for financial restructuring of public corporations, Chapter XI provided "for arrangements and compositions for corporations, partnerships and individuals," and Chapter XII contained "the procedures for arrangements for noncorporate entities involved in real estate." H.R. Rep. No. 595 at 221, *reprinted in* 1978 U.S. Code Cong. & Admin. News at 6181. Chapter 11 of the Bankruptcy Code represents the consolidation of these chapters into a "single chapter for all business reorganizations." S. Rep. No. 989 at 9, *reprinted in* 1978 U.S. Code Cong. & Admin. News at 5795.[12] Nothing in the legislative history specifically indicates that this consolidation was intended to provide a benefit for consumer debtors. On the contrary, as remarked above (see Part III), the House Report clearly states that consumer debtors may seek relief only under Chapters 7 and 13.

While contending that consumer debtors could use former Chapter XI, Petitioner concedes that they were expressly excluded from relief under former Chapter X. Pet. Br. at 14. Thus, Congress would have been required to choose between conflicting provisions in consolidating the business reorganization chapters. *See, United Savings Ass'n. of Texas v. Timbers of Inwood Forest Assoc., Ltd.*, 484 U.S. 365, 380-381 (1988) (in replacing Chapters X, XI and XII with a single business reorganization chapter, "Congress would have been faced with the choice between adopting the rule from Chapters X and XII or

[12] The Senate Report states that "Chapter 11 replaces chapters X, XI and XII of the Bankruptcy Act[.] Chapter 11 also includes special provisions for railroads in view of the impact of regulatory laws on railroad debtors and replaces section 77 of the Bankruptcy Act." S. Rep. No. 989 at 9, *reprinted in* 1978 U.S. Code Cong. & Admin. News at 5795.

the asserted alternative rule from Chapter XI").[13] There is no basis for "presuming" that consumer debtors are eligible for relief under Chapter 11 simply because they were eligible for relief under one, but not all, of the predecessor provisions. *See, Timbers of Inwood Forest*, 484 U.S. at 381. Indeed, given the legislative history discussed above—particularly the statement in the House Report demonstrating that Chapters 7 and 13 are the only chapters available to consumer debtors—the conclusion must be that Congress did not intend that consumer debtors be given relief under Chapter 11.

VI. POLICY CONSIDERATIONS COUNSEL AGAINST ALLOWING CONSUMER DEBTORS TO USE CHAPTER 11

As the Senate and House Reports articulate, Chapter 11's purpose is to permit business debtors to reorganize and restructure their debts in order to return to a viable state. Towards this end, the assets used in the business's operation are preserved to the extent necessary to effectuate reorganization, and the proceeds produced by those assets are used to repay creditors. Permitting businesses to reorganize promotes the public interest in preserving jobs and protecting investors. No such pur-

[13] In *Timbers of Inwood Forest*, petitioner argued that 11 U.S.C. § 362(d)(1) entitles an undersecured creditor to postpetition interest. In support, he contended that former Chapter XI gave an undersecured creditor relief from the automatic stay provision by permitting him to foreclose and that Congress would not have withdrawn this right without any indication of intent to do so in the legislative history unless it provided an adequate substitute in the form of interest during the stay. This Court rejected that argument, observing that, even assuming an undersecured creditor had an absolute entitlement to foreclosure under former Chapter XI, no such right existed under former Chapters X and XII. The Court concluded that nothing could be read into the silence of the legislative history because, in consolidating the chapters, Congress could have adopted the approach of Chapter XI or the alternative approach of Chapters X and XII. *Timbers of Inwood Forest*, 484 U.S. at 380-381.

pose is served by allowing an individual nonbusiness debtor to proceed under Chapter 11. A consumer debtor has no business-related assets capable of generating income and no employees or investors to be protected.

Moreover, the earnings from services performed personally by an individual Chapter 11 debtor after commencement of the case are exempt from the bankrupt estate. 11 U.S.C. § 541(a)(6); *In re Fitzsimmons*, 725 F.2d 1208, 1211 (9th Cir. 1984). Thus a consumer debtor invoking Chapter 11 would be able to shield both his disposable income and his non-exempt personal assets from his creditors. To allow this, however, would provide such a debtor far more protection than Chapter 13 —which does not protect disposable income—or Chapter 7—which does not protect non-exempt personal assets. There certainly is no indication that Congress intended to provide a consumer debtor such expansive protection through Chapter 11. Indeed, the legislative history described above establishes the contrary.

Respondent contends that consumer debtors should be permitted to obtain relief under Chapter 11 because Congress prefers reorganization over liquidation. Resp. Br. at 14-17. In support of this contention, Respondent cites 11 U.S.C. § 706(a) and 707(b). Pursuant to Section 706(a), a debtor is given a one-time, absolute right to convert a Chapter 7 liquidation case to a case under Chapters 11, 12 or 13. Respondent asserts that this conversion right reflects a policy favoring reorganization over liquidation. This analysis is flawed because a debtor under Chapter 11, 12 or 13 is given the same right to convert a reorganization case to a Chapter 7 liquidation case. *See* 11 U.S.C. §§ 1112(a), 1208(a) and 1307(a). These conversion rights no more reflect a policy favoring reorganization than a policy favoring liquidation.

Section 707(b) authorizes a court to dismiss a Chapter 7 liquidation case filed by a consumer debtor if granting of relief would constitute a "substantial abuse of the

provisions of this chapter." As observed, courts have invoked this provision to dismiss Chapter 7 consumer cases where the debtor has the financial resources to repay his creditors. *In re Krohn*, 886 F.2d 123 (6th Cir. 1989); *In re Walton*, 866 F.2d 981 (8th Cir. 1989); *In re Kelly*, 841 F.2d 908 (9th Cir. 1988). Rather than manifesting a policy favoring reorganization over liquidation as Respondent contends (Resp. Br. at 14), this provision simply authorizes courts to *dismiss* and deny a fresh start to a consumer debtor whose financial situation does not warrant the discharge of his debts in exchange for the liquidation of his assets. *In re Krohn*, 886 F.2d at 126-127.

Petitioner asserts that permitting consumer debtors to use Chapter 11 is consistent with the structure of the Bankruptcy Code, which is designed to provide debtors alternative remedies. Pet. Br. at 20-27. Barring consumer debtors from using Chapter 11, however, does not generally deny them a choice of remedies. Consumer debtors normally are eligible to proceed under either Chapter 7 or Chapter 13. The fact that consumer debtors who do not meet the Chapter 13 eligibility requirements may be forced to liquidate under Chapter 7 is no reason to permit them to file under Chapter 11. "[B]ankruptcy is not the only method available to a debtor for the adjustment of his relationship with his creditors." *United States v. Kras*, 409 U.S. 434, 445 (1973). Moreover, Congress obviously made a policy decision that consumer debtors with debts exceeding certain limits or who had no regular income *should not* be able to utilize Chapter 13. It also is reasonable to assume that Congress decided that eligible consumer debtors should use Chapter 13—which requires use of disposable postpetition income to pay their debts—and not Chapter 11, which would allow protection of both non-exempt assets *and* postpetition income earned by personal services.[14]

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[14] 11 U.S.C. § 541(a)(6).

Finally, we must note the hardships on bankruptcy and higher courts that a ruling allowing consumer debtors to reorganize under Chapter 11 could entail. The courts might well be flooded with suspect, jerry-built plans, which eventually would prove unworkable, from consumer debtors who seek to use Chapter 11 to protect both their non-exempt assets and their postpetition income (which Chapter 13 does *not* safeguard). The courts evidently have enough to do in ruling on Chapter 11 *business* reorganization plans, most of which fail.[15] To impose an additional burden on the courts does not seem warranted, especially when most consumer debtors can avail themselves of the debt restructuring provisions of Chapter 13.

CONCLUSION

For the foregoing reasons, this Court should affirm the decision of the Eighth Circuit Court of Appeals.

Respectfully submitted,

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[15] According to Respondent, almost 90 percent of Chapter 11 reorganizations fail. Resp. Br. at 18, n.10.